

AR48

# COMTECH

GROUP INTERNATIONAL LIMITED

## 1971 ANNUAL REPORT





## *Directors*

Robert Bellamy

Michel Bourbonnais

James E. Houston

Eugene A. Kolaczynski

Edward K. Loyst

Donald M. McPhail

Sinclair M. Stevens

## *Officers*

Sinclair M. Stevens, Chairman

Donald M. McPhail, President

Lionel T. Colman, Treasurer

Noreen M. Stevens, Secretary

## *Annual General Meeting*

The 1971 Annual and General Meeting of Shareholders of Comtech Group International Limited will be held in the Prince Edward Island Room of the Royal York Hotel in Toronto, at 10:00 a.m. on October 29, 1971.

**COMTECH GROUP INTERNATIONAL LIMITED**  
50 Lesmill Road, Don Mills, Ontario  
**NOTICE OF ANNUAL AND GENERAL MEETING OF SHAREHOLDERS**

NOTICE is hereby given that the annual and general meeting of the shareholders of Comtech Group International Limited will be held in the Prince Edward Island Room, Royal York Hotel, Toronto, Ontario, on Friday, the 29th day of October, 1971 at the hour of 10 o'clock in the forenoon (Toronto time) for the following purposes:

- (a) To receive the consolidated financial statements of the Corporation and its subsidiaries for the financial year ended the 30th day of June, 1971 together with the report of the Corporation's auditors thereon and the report of the directors;
- (b) To consider and if thought advisable to confirm subject to such amendments or additions as may be approved at the meeting the by-law passed by the directors on the 1st day of October, 1971 respecting the indemnification of directors and officers; a copy of such by-law accompanies this notice;
- (c) To elect directors;
- (d) To appoint auditors and authorize the directors to fix their remuneration;
- (e) To transact such further and other business as may properly come before this meeting or any adjournment thereof.

DATED at Toronto this 7th day of October, 1971.

BY ORDER OF THE BOARD  
Noreen M. Stevens,  
Secretary.



# COMTECH GROUP INTERNATIONAL LIMITED

## INFORMATION CIRCULAR

AS OF OCTOBER 5, 1971

### **SOLICITATION OF PROXIES**

This Information Circular is furnished in connection with the solicitation by management of Comtech Group International Limited (the "Corporation") of proxies to be used at the annual and general meeting of shareholders of the Corporation to be held at the time and place and for the purposes set forth in the enclosed notice of meeting. It is expected that the solicitation will be by mail and may be supplemented by telephone. The cost of solicitation will be borne by the Corporation.

### **APPOINTMENT AND REVOCATION OF PROXIES**

The persons named in the enclosed form of proxy are directors of the Corporation. A SHAREHOLDER DESIRING TO APPOINT SOME OTHER PERSON TO REPRESENT HIM AT THE MEETING MAY DO SO BY INSERTING SUCH PERSON'S NAME IN THE BLANK SPACE PROVIDED IN THE FORM OF PROXY AND STRIKING OUT THE NAME OF MANAGEMENT'S NOMINEES OR BY COMPLETING ANOTHER PROPER FORM OF PROXY AND IN EITHER CASE DELIVERING THE COMPLETED PROXY TO THE SECRETARY OF THE CORPORATION OR THE SCRUTINEERS AT THE MEETING.

A shareholder who has given a proxy may revoke it either (a) by signing a proxy bearing a later date and delivering it to the Secretary of the Corporation or (b) as to any matter on which a vote shall not already have been cast pursuant to the authority conferred by such proxy, by signing written notice of revocation and delivering it to the Secretary of the Corporation or the Chairman of the meeting.

### **EXERCISE OF DISCRETION BY PROXIES**

The persons named in the enclosed form of proxy will vote the shares in respect of which they are appointed in accordance with the direction of the shareholders appointing them. IN THE ABSENCE OF SUCH DIRECTION SUCH SHARES WILL BE VOTED FOR THE ELECTION OF DIRECTORS, FOR THE APPOINTMENT OF AUDITORS AND FOR CONFIRMATION OF THE BY-LAW RESPECTING INDEMNIFICATION OF OFFICERS AND DIRECTORS AS STATED UNDER THOSE HEADINGS IN THIS CIRCULAR. THE ENCLOSED FORM OF PROXY CONFERS DISCRETIONARY AUTHORITY UPON THE PERSONS NAMED THEREIN WITH RESPECT TO AMENDMENTS OR VARIATIONS TO MATTERS IDENTIFIED IN THE NOTICE OF MEETING AND WITH RESPECT TO OTHER MATTERS WHICH MAY PROPERLY COME BEFORE THE MEETING. AT THE TIME OF PRINTING THIS CIRCULAR, THE MANAGEMENT OF THE CORPORATION KNOWS OF NO SUCH AMENDMENT, VARIATIONS OR OTHER MATTERS TO COME BEFORE THE MEETING OTHER THAN THE MATTERS REFERRED TO IN THE NOTICE OF MEETING.

### **VOTING SHARES**

(a) As at October 5th, 1971 the following shares of the Corporation were issued and outstanding: 4,490 5% first preference shares each having one vote, 55,482 3% second preference shares each having one vote and 757,363 common shares each having one vote. The aggregate number of votes attaching to all the outstanding shares is 817,335. Shareholders of record at the commencement of the meeting are entitled to vote at the meeting.

(b) Notice of Meeting, together with an instrument of proxy and an Information Circular, will be mailed to each shareholder of record as of October 7th, 1971.

(c) The directors and senior officers of the Corporation do not know of any person or company beneficially owning directly or indirectly shares carrying more than ten percent (10%) of the voting rights attached to all shares of the Corporation.

## ELECTION OF DIRECTORS

The following are the present directors of the Corporation and the nominees for election at this shareholder's meeting; the term of office in each case is until the next annual meeting of shareholders or until their successors in office are elected or appointed:

<u>Name</u>	<u>Office Held with the Corporation</u>	<u>Date Became a Director</u>	<u>Common Shares Owned</u>
Robert Bellamy	Director	October 15, 1969	1,500
Michel Bourbonnais	Director	October 15, 1969	700
James Edward Houston	Director	June 16, 1969	37,100
Eugene Kolaczynski	Director	April 23, 1971	1,000
Edward Kenneth Loyst	Director	December 7, 1970	100
Donald Murdo McPhail	Director and President	June 16, 1969	21,500
Sinclair McKnight Stevens	Director and Chairman	October 15, 1969	68,444

Robert Bellamy is an investment dealer with A. E. Ames & Company Limited of Toronto, Ontario.

Michel Bourbonnais is Vice-President of RAM Investments Inc. of Montreal, Quebec.

James Edward Houston is an investment dealer with A. E. Osler Company Limited, Toronto, Ontario.

From December, 1967 to January 1, 1971, Eugene Kolaczynski was general manager of Administration & Finance Inc. of Montreal, now named Comtech Limitee, and since January 1, 1971 he has been and continues to be Vice-President thereof; prior to December, 1967, he was Controller of Canadian Printing and Lithographing Limited of Montreal.

Edward Kenneth Loyst is the President of Living Lighting Limited of Toronto, Ontario.

Donald Murdo McPhail is the President of the Corporation.

Sinclair McKnight Stevens is a partner of the law firm of Stevens Charlebois & Stevens, Toronto, Ontario.

### NOTE:

The information as to shares beneficially owned by directors not being within the knowledge of the Corporation has been furnished by the respective directors individually.

## REMUNERATION OF DIRECTORS AND SENIOR OFFICERS

The aggregate remuneration paid or payable during the fiscal year 1971 by the Corporation to its directors and senior officers was \$99,859.

## INTEREST OF MANAGEMENT IN MATERIAL TRANSACTIONS

On April 23rd, 1971, the Corporation entered into a share purchase agreement with five of its senior full-time employees to purchase an aggregate of 9,300 common shares at \$1.40 per share. On April 23rd, 1971 the Corporation also entered into a five-year incentive stock option plan with full-time employees for 4,250 common shares at \$1.40 per share exercisable on a cumulative basis at the rate of twenty percent (20%) per year. Thirty days prior to April 23rd, 1971, the price range of the Corporation's common shares on the Toronto Stock Exchange was \$1.60 to \$1.75.



During 1971 full-time employees of the Corporation exercised options previously granted under incentive stock option agreements as follows:

<u>Number of Common Shares</u>	<u>Purchase Price per share</u>	<u>Calendar Quarter during which shares purchased</u>	<u>Price Range of Shares on Toronto Stock Exchange</u>
600	\$1.00	July 1/70 – Sept. 30/70	\$1.10 – \$1.80
1,100	\$1.00	Oct. 1/70 – Dec. 30/70	\$1.60 – \$2.10
1,000	\$1.00	Jan. 1/71 – Mar. 31/71	\$1.60 – \$2.00
1,100	\$1.00	Apr. 1/71 – June 30/71	\$1.60 – \$2.55

The Corporation has sold \$200,000 of 7 1/2% convertible unsecured debentures at a four percent (4%) discount from face value maturing June 30th, 1976 to the following: Donald Murdo McPhail \$10,000, Sinclair McKnight Stevens \$35,000, Lionel T. Colman, the Treasurer of the Corporation, \$15,000, Michel Bourbonnais \$50,000, James Edward Houston \$65,000, Noreen M. Stevens, the Secretary of the Corporation, \$25,000. These debentures are convertible into common shares at the price of \$2.00 until June 30th, 1973, \$3.00 until June 30th, 1974, \$4.00 until June 30th, 1975 and \$5.00 until June 30th, 1976.

#### **APPOINTMENT OF AUDITORS**

The persons named in the enclosed form of proxy intend to vote for the re-appointment of Messrs. Laventhol Krekstein Horwath & Horwath of Toronto as auditors of the Corporation to hold office until the next annual meeting of shareholders. Messrs. Laventhol Krekstein Horwath & Horwath have been auditors of the Corporation since 1967.

#### **PARTICULARS OF MATTERS TO BE ACTED UPON**

By-law regarding indemnification of officers and directors.

The Business Corporations Act (Ontario) nullified as of January 1, 1971 any by-law indemnifying directors and officers. The new by-law is drafted to conform to the requirements of the aforesaid statute.

#### **BY-LAW RESPECTING INDEMNIFICATION OF OFFICERS AND DIRECTORS**

NOW THEREFORE BE AND IT IS HEREBY ENACTED as a by-law of Comtech Group International Limited that:

- (1) Subject to subsection (2) of this by-law every director and officer of the Corporation and his heirs, executors, administrators and other legal personal representatives shall from time to time be indemnified and saved harmless by the Corporation from and against
  - (a) any liability and all costs, charges and expenses that he sustains or incurs in respect of any action, suit or proceeding that is proposed or commenced against him for or in respect of anything done or permitted by him in respect of the execution of the duties of his office; and
  - (b) all other costs, charges and expenses that he sustains or incurs in respect of the affairs of the Corporation.
- (2) No director or officer of the Corporation shall be indemnified by the Corporation in respect of any liability, costs, charges or expenses that he sustains or incurs in or about any action, suit or other proceeding as a result of which he is adjudged to be in breach of any duty or responsibility imposed upon him under The Business Corporations Act, 1970 (Ontario) or under any other statute unless, in an action brought against him in his capacity as director or officer, he has achieved complete or substantial success as a defendant.
- (3) This by-law shall come into effect on the date of its enactment by the Board of Directors and upon becoming effective the provisions of any prior by-law inconsistent herewith shall be automatically repealed.

DATED this 1st day of October, 1971.

## *Highlights*

### *of Continuing Operations*

	<u>1971</u>	<u>1970</u>	<u>Increase (Decrease)</u>
Computer service revenue .....	\$1,169,146	\$ 948,705	23%
Package revenue .....	\$ 744,780	\$ 404,820	83%
Costs and expenses .....	\$1,101,676	\$1,198,186	(8%)
Income (loss) before provision for taxes .....	\$ 72,985	(\$ 26,211)	
Income (loss) .....	\$ 43,903	(\$ 13,112)	
Per common share			
Income before taxes .....	10¢	(4¢)	
Income .....	6¢	(2¢)	
Average number of shares outstanding .....	748,463	698,428	



## President's Report

### TO OUR SHAREHOLDERS:

Our continuing increase in revenue and a decrease in expenses have resulted in your Company showing income on continuing operations of \$43,903 (6¢ per share) for the year ended June 30, 1971 compared with a loss of \$13,112 (2¢ loss per share) in 1970. Computer service revenue has risen by 23% to \$1,169,146 compared with \$948,705 for 1970. Costs, on the other hand, fell 8% in 1971 to \$1,101,676 compared with \$1,198,186 the year before.

Package revenue jumped 83% to \$744,780 compared with \$404,820 last year. Custom work declined. 1971's improved results reflect Comtech's policy of orienting its service to package-type activities and away from general or custom work.

For comparison purposes, certain items have been extracted from the statement of source and application of funds and summarized as follows:

	1971	1970
Funds provided by continuing operations	\$ 247,857	\$ 99,031
Charges to systems and data centre development costs	187,613	159,466
Net inflow (outflow)	\$ 60,244	(\$ 60,435)

This favourable trend will continue quarter by quarter for the following reasons:

- (a) Each dollar of additional revenue now has a high profit content since we have passed the critical break-even point in our Toronto and Montreal centres;
- (b) Our computer equipment becomes less expensive each month as the principal owing is paid down which in turn lowers our interest costs.
- (c) The Company's account base (now over 600) and sales momentum is snowballing monthly into additional revenue from existing customers and new revenue from others.
- (d) Comtech's running operations continually become more efficient in terms of computer utilization, data handling and client service.

With our expanding operations, it was felt that further working capital for the Company was desirable and we are pleased to report that a \$200,000, 7½% convertible debenture has been placed which is reflected in the enclosed financial statements. Partly due to this financing,



our working capital position has improved by \$58,815 during the year. With respect to \$72,000 of our debt, the Company has negotiated promissory notes due on a monthly basis until June 15, 1972. This will also provide additional flexibility in our working capital position.

We have segregated from other liabilities the principal payments on computer equipment due over the next twelve months as these are monthly amounts due on our equipment (like rent). This also highlights the favourable position which is now developing in our remaining long-term debt (Note 7). It would cost Comtech over \$195,000 per year to rent its present equipment if we did not own it. After 1972 we will owe only \$247,149 on such equipment or the equivalent of 15 months' rent. After that we will own the equipment outright and Comtech will experience a sharp positive increase in its cash flow.

An important event during the year was the sale of the Fibre Products division. Your directors considered this to be a prudent move in light of technological changes in the equipment automotive supply field, rendering a severe handicap to this division. The loss incurred by the Company in selling the division itself is reflected as an extraordinary item in our 1971 statements. In future years, we will not be carrying this operating or extraordinary loss. With this sale, our Company is now solely in the computer service field.

We intend to continue our policy of concentrating on package oriented data processing activities which have high profit margins. We insist that a products profitability be demonstrated before its sale is promoted or fixed overhead is assumed. We believe our policy is proving sound and we intend to rigidly enforce it.

Recent changes in governmental requirements have been fully considered and provided for in our Paymaster program which should give us a further competitive advantage.

This year we have added to our payroll and job costing packages, an accounts receivable system. Currently this new product is being marketed to our existing accounts and has proven competitive and profitable. Shortly, we expect to begin full-scale marketing of this new package.

In 1971 the Company made a profit in Canada which was lessened by our operations in the

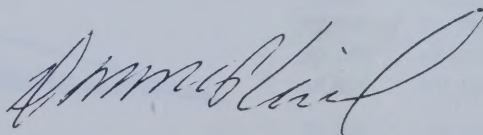
U.S.A. where we had a loss. In Canada the bulk of our business was package oriented while the reverse was true in the U.S.A. Accordingly, late in the year we re-arranged our Boston operation so that it is now 90% package oriented. With this change we no longer needed to own our own computer. The Company therefore disposed of the Boston computer equipment by agreement with the computer supplier to take back the equipment (see Note 3). With our package orientation and by renting identical equipment without a long-term lease and making other overhead reductions, the Boston centre is now running at a near break-even level.

The past twelve to twenty-four months have been a difficult period for computer and data processing companies. Virtually all companies which have entered the field in Canada have sustained heavy losses in spite of being underwritten, in the aggregate, with over \$50 million in public funds. Comtech has relied on internally generated funds or on private placements rather than resorting to the public market. We have concentrated on developing saleable products that can be produced profitably: not on spending money in experimentations. We intend to continue this approach.

We are pleased that Mr. Paul McKenzie has been retained by us to assist in our development of the Company's sales area. Mr. McKenzie has had vast experience in the training and managing of sales forces in the accounting services field. He is now working with our Company's sales personnel.

We would be remiss if we did not take this opportunity to thank all Comtech employees for their co-operation during the year. They are our greatest resource.

On behalf of the board of directors.



President

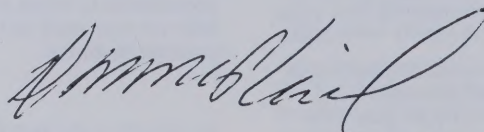
October 1, 1971

# COMTECH GROUP INTERNATIONAL LIMITED AND SUBSIDIARIES

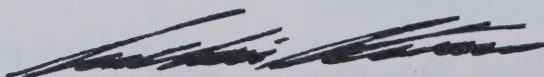
## ASSETS

	1971	1970
		(Restated)
<b>CURRENT ASSETS</b>		
Cash .....	\$ 18,719	\$ 17,214
Subscriptions receivable (Note 8) .....	154,180	—
Accounts receivable .....	193,249	346,154
Inventories, at cost .....	19,098	148,531
Prepayments and advances .....	42,640	62,267
Current maturities on debenture receivable .....	—	24,000
	<u>427,886</u>	<u>598,166</u>
<b>FIXED ASSETS (Note 3)</b>		
Cost .....	884,880	2,182,168
Accumulated depreciation .....	254,419	575,622
	<u>630,461</u>	<u>1,606,546</u>
<b>SYSTEMS AND DATA CENTRE DEVELOPMENT COSTS (Note 4)</b> .....	371,911	221,734
<b>OTHER ASSETS, at cost (Note 5)</b> .....	10,225	167,387
<b>EXCESS OF COST OF INVESTMENT IN SUBSIDIARIES OVER NET ASSETS ACQUIRED (Note 1)</b> .....	616,758	611,029

Signed on behalf of the Board:



Director



Director

<u>\$2,057,241</u>	<u>\$3,204,862</u>
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# Consolidated Balance Sheet as at June 30, 1971

## LIABILITIES

	1971	1970
<b>CURRENT LIABILITIES</b>		(Restated)
Bank indebtedness and other term loans (Note 6) .....	\$ 123,645	\$ 226,655
Accounts payable and accrued liabilities .....	201,630	403,038
Current liabilities before computer equipment payments .....	325,275	629,693
Amount due on computer equipment, paid August 16, 1971 .....	75,000	—
Monthly instalments due over next twelve months (Note 7) .....	201,665	201,342
	<u>601,940</u>	<u>831,035</u>
<b>LONG-TERM DEBT</b>		
Notes payable on computer equipment (Note 7) .....	247,149	732,280
7½% convertible debenture, due June 30, 1976 (Note 8) .....	200,000	—
<b>DEFERRED INCOME TAXES</b> .....	3,050	—
<b>DEFERRED INCOME</b> .....	—	17,650
	<u>1,052,139</u>	<u>1,580,965</u>

## SHAREHOLDERS' EQUITY

### CAPITAL STOCK

#### Authorized

- 14,490 5% First preference shares, \$10 par value, cumulative,  
redeemable at \$10.20 a share
- 157,482 3% Second preference shares, \$1 par value, non-cumulative,  
redeemable at par
- 2,000,000 Common shares, \$1 par value

#### Issued

4,490 5% Preference shares .....	44,900	44,900
55,482 3% Preference shares .....	55,482	55,482
757,363 Common shares (Note 9) .....	757,363	744,263
	<u>857,745</u>	<u>844,645</u>
<b>CONTRIBUTED SURPLUS</b> (Note 10) .....	116,857	681,851
<b>RETAINED EARNINGS</b> .....	30,500	97,401
	<u>1,005,102</u>	<u>1,623,897</u>
	<u>\$2,057,241</u>	<u>\$3,204,862</u>

**COMTECH GROUP INTERNATIONAL LIMITED** AND SUBSIDIARIES*Consolidated Statement of Income from Continuing Operations*

FOR THE YEAR ENDED JUNE 30, 1971

	<u>1971</u>	<u>1970</u> (Restated)
<b>REVENUES</b>		
Computer services		
Package processing and related services .....	\$ 744,780	\$ 404,820
Custom work and other .....	424,366	543,885
	<u>1,169,146</u>	<u>948,705</u>
Charter fees and royalties .....	5,515	223,270
	<u>1,174,661</u>	<u>1,171,975</u>
 <b>COSTS AND EXPENSES</b>		
Salaries and benefits .....	357,671	449,890
Computer operations .....	444,392	389,722
Marketing and administration .....	299,613	358,574
	<u>1,101,676</u>	<u>1,198,186</u>
Income (loss) before taxes .....	<u>72,985</u>	<u>(26,211)</u>
Provision for income taxes and minority interest		
Income taxes .....	28,050	(14,007)
Minority interest .....	1,032	908
	<u>29,082</u>	<u>(13,099)</u>
<b>INCOME (LOSS) ON CONTINUING OPERATIONS</b> .....	<u>\$ 43,903</u>	<u>(\$ 13,112)</u>



*Consolidated Statement of Income and Retained Earnings*

FOR THE YEAR ENDED JUNE 30, 1971

	1971	1970 (Restated)
Income (loss) on continuing operations (see statement) .....	\$ 43,903	(\$ 13,112)
Income (loss) on discontinued operations (Note 2) .....	(70,343)	16,314
Income (loss) including loss on discontinued operations before extraordinary items .....	(26,440)	3,202
Extraordinary items		
Loss on disposal of Fibre Products business (Note 2) .....	(487,351)	—
Profit (loss) on disposal of fixed assets (Note 3) .....	(136,124)	127,829
Reduction of income taxes due to application of tax loss carry forwards ..	14,300	6,900
Settlement with a vendor of a subsidiary acquired .....	—	(8,333)
	(609,175)	126,396
<b>NET INCOME (LOSS)</b> .....	<b>(\$ 635,615)</b>	<b>129,598</b>
Retained earnings at start of year		
As previously reported .....	79,645	62,734
Prior years' adjustments (Note 4)		
Organization and finance expenses .....	—	(94,931)
Amortization of data centre development costs .....	17,756	—
	97,401	(32,197)
	(538,214)	97,401
Transfer from contributed surplus (Note 10) .....	568,714	—
<b>RETAINED EARNINGS AT END OF YEAR</b> .....	<b>\$ 30,500</b>	<b>\$ 97,401</b>

**COMTECH GROUP INTERNATIONAL LIMITED AND SUBSIDIARIES**

*Consolidated Statement of Source and Application of Funds*

FOR THE YEAR ENDED JUNE 30, 1971

	1971	1970 (Restated)
<b>SOURCE OF FUNDS</b>		
Continuing operations		
Income (loss) on continuing operations	\$ 43,903	(13,112)
Charges not requiring funds		
Depreciation on fixed assets	139,820	70,494
Amortization of deferred charges	35,452	39,596
Provision for deferred income tax and minority interest	28,682	2,053
<b>FUNDS PROVIDED BY CONTINUING OPERATIONS</b>	<b>247,857</b>	<b>99,031</b>
Debenture receivable discharged against Adjustment Assistance Board debt	138,000	—
Issue of common shares		
On stock purchase and exercise of stock options	16,820	—
In exchange for shares of subsidiary	—	60,000
Issue of 7½% convertible debenture	190,975	—
Increase in notes on computer equipment	—	226,497
Proceeds on sale of fixed assets (Note 3)	221,757	207,273
Proceeds on sale of subsidiary, Fibre Products	74,743	—
	<b>890,152</b>	<b>592,801</b>
<b>APPLICATION OF FUNDS</b>		
Operations of Fibre Products to date of disposal		
Loss on discontinued operations (Note 2)	70,343	(16,314)
Depreciation	(9,533)	(30,394)
	60,810	(46,708)
Costs of winding up Fibre Products premises	77,338	—
Funds applied to discontinued operations and extraordinary items	138,148	(46,708)
Purchase of fixed assets	4,183	458,369
Investment in shares of subsidiaries, less working capital at dates of acquisition	16,815	307,635
Systems and data centre development costs		
Package programs	30,175	76,155
Data centre development	157,438	83,311
Retirement of long-term debt		
Adjustment Assistance Board secured debenture (Note 2)	138,000	24,000
Notes on computer equipment (Note 3)	335,469	107,797
Other	8,800	57,333
Miscellaneous	2,309	2,692
	<b>831,337</b>	<b>1,070,584</b>
<b>INCREASE (DECREASE) IN WORKING CAPITAL POSITION</b>	<b>58,815</b>	<b>(477,783)</b>
	<b>\$ 890,152</b>	<b>\$ 592,801</b>



## Auditors' Report

To the Shareholders of  
Comtech Group International Limited

We have examined the consolidated balance sheet of Comtech Group International Limited and its subsidiaries as at June 30, 1971 and the consolidated statements of income and retained earnings and source and application of funds for the year then ended. Our examination included a general review of the accounting procedures and such tests of accounting records and other supporting evidence as we considered necessary in the circumstances.

In our opinion, these consolidated financial statements present fairly the financial position of the companies as at June 30, 1971 and the results of their operations and the source and application of their funds for the year then ended in accordance with generally accepted accounting principles applied, after giving retroactive effect to the change in accounting method of amortization of systems and data centre development costs, as explained in Note 4 to the consolidated financial statements, on a basis consistent with that of the preceding year.

Toronto, Ontario  
September 28, 1971

*Solentol Kreitzstein Horwath & Horwath*  
Chartered Accountants

## Notes to 1971 Consolidated Financial Statements

### 1. ACQUISITIONS AND PRINCIPLES OF CONSOLIDATION

The Company owns the following principal subsidiaries:

<u>Name of Subsidiary</u>	<u>Date Acquired</u>	<u>Percentage Owned</u>
Comtech Group Limited	June 3, 1969	100%
Subsidiaries of Comtech Group Limited		
Comtech (Central) Limited	March 30, 1968	100%
Comtech Limitée	August 7, 1968	100%
Commercial Computer Services Inc.	November 3, 1969	90%
Comtech New England Inc.	May 29, 1970	100%

The subsidiaries of Comtech Group Limited were acquired as purchases. The excess of cost price over underlying net assets at the date of acquisition has been reflected as "excess of cost of investment in subsidiaries over net assets acquired." The operations of such companies acquired during the year have been included in the accompanying financial statements from the dates of acquisition. It is the Company's policy not to amortize excess of cost of investment in subsidiaries over net assets acquired since management is of the opinion that there has been no diminution of value. However, certain charges to income, such as settlements with vendors of subsidiaries, provisions for deferred income tax and minority interest, have been credited to this account since such costs have been treated as a recovery of part of the purchase price. The total amount so charged to income is \$11,332 in 1971 (\$11,341 in 1970) and \$34,340 cumulative to date.

### 2. SALE OF SUBSIDIARY

In December 1970, the Company completed the sale of its automotive parts manufacturing business ("Fibre Products"). During the 5 months of operations to November 30, 1970, sales of Fibre Products amounted to \$221,725 compared with \$1,559,030 for the 12 months ended June 30, 1970. The 5 month operating loss of \$70,343 is shown separately as a loss on discontinued operations and the 1970 figures have been reclassified to conform with this presentation.

The \$487,351 loss on disposal of this business includes \$77,338 of net costs of operating as head tenant at the Fibre Products factory since the purchaser of Fibre Products agreed to lease only part of the premises. This includes the estimated net costs until termination of the lease. The loss on disposal is reflected as an extraordinary item.

In conjunction with the sale of Fibre Products, the Company was discharged from its debenture payable to the Adjustment Assistance Board in consideration of the assignment of title to the debenture receivable on identical terms.

# COMTECH GROUP INTERNATIONAL LIMITED AND SUBSIDIARIES

## 3. FIXED ASSETS

	1971			1970
	Cost	Accumulated Depreciation	Net	Net
Machinery and equipment .....	\$ —	\$ —	\$ —	\$ 471,688
Computer equipment .....	732,355	176,225	556,130	1,032,773
Magnetic tapes .....	35,486	16,709	18,777	24,227
Furniture and office equipment .....	87,308	42,510	44,798	57,056
Leasehold improvements .....	25,983	16,354	9,629	13,543
Vehicles .....	3,748	2,621	1,127	7,259
	<u>\$ 884,880</u>	<u>\$ 254,419</u>	<u>\$ 630,461</u>	<u>\$ 1,606,546</u>

The Company depreciates its fixed assets on a straight-line basis over their estimated useful lives. Total depreciation recorded on fixed assets during 1971 was \$149,353 (\$100,888 in 1970).

As at June 30, 1971, the Company disposed of the computer equipment at its Boston data centre by agreement with the computer supplier to take back the equipment at the value represented by the unmatured notes payable of \$215,434 which resulted in a loss of \$136,124. That data centre is currently renting identical computer equipment without long-term lease commitment.

## 4. SYSTEMS AND DATA CENTRE DEVELOPMENT COSTS

	Amortized During Year	Unamortized 1971	Balance 1970
			(Restated)
Package programs .....	\$ 31,054	\$ 121,807	\$ 124,670
Data centre development .....	4,398	250,104	97,064
	<u>\$ 35,452</u>	<u>\$ 371,911</u>	<u>\$ 221,734</u>

Package programs are amortized on a straight-line basis over a five-year period, commencing upon completion of each program for marketing.

In May, 1970, the Company acquired the Comtech New England Inc. data centre. Certain costs (including salaries, operations, sales and administration) in connection with the transition of this centre into the package processing business and opening up new geographical areas have been deferred as "data centre development" costs. The sales development costs capitalized in 1970 have now been included in this category.

In prior years, sales development costs were amortized on a straight-line basis over a 24 month period commencing in the fourth month after incurrence of such costs. Commencing with 1971, the Company has changed its method of amortizing data centre development costs to a five year period using the reverse sum-of-the-years' digits method (1/15, 2/15, 3/15, 4/15, 5/15) once each subject data centre reaches break-even on a cash flow basis. As a result of this change the 1970 figures have been restated by a reduction in amortization of deferred charges of \$17,756 thereby increasing 1970 net income by the same amount.

## 5. OTHER ASSETS, AT COST

	1971	1970
Debenture receivable (Note 2) .....	\$ —	\$ 138,000
Notes receivable .....	—	14,900
Debenture issue expense .....	9,025	—
Patents .....	—	12,356
Miscellaneous .....	1,200	2,131
	<u>\$ 10,225</u>	<u>\$ 167,387</u>

Deferred debenture issue expense represents a discount of \$8,000 and expenses of \$1,025 in conjunction with the 7½% convertible debentures (Note 8). These will be amortized on a straight-line basis over the next five years.

## 6. BANK INDEBTEDNESS

Accounts receivable amounting to \$197,366 have been pledged for bank indebtedness.



# COMTECH GROUP INTERNATIONAL LIMITED AND SUBSIDIARIES

## 7. NOTES PAYABLE ON COMPUTER EQUIPMENT

	1971	1970
Secured debentures, payable to Adjustment Assistance Board, \$2,000 principal monthly to March 1977; interest payable at the rate of 7½% per annum on \$14,000 and 6% per annum on remainder (Note 2)	\$ —	\$ 162,000
Lien notes payable on computer equipment (at interest approximating prime bank borrowing rates)		
Monthly principal instalments of \$3,881 to 1973	91,680	138,248
Monthly principal instalments of \$6,122 to 1975	275,504	348,970
8¾% Lien notes payable on computer equipment (Note 3)	—	272,004
Other debt	—	12,400
Promissory notes to computer supplier (at interest 2% above prime bank rates) originating from lien notes		
Monthly principal instalments of \$7,200 to 1972	81,630	—
	448,814	933,622
Less current maturities	201,665	201,342
	<u>\$ 247,149</u>	<u>\$ 732,280</u>

The Company has followed the approach of purchasing its major equipment (rather than leasing) which has resulted in the inclusion under current liabilities of \$201,665 representing the next 12 months of principal payments on computer equipment.

The aggregate amounts of payments required for retirement provisions in each of the next five years are as follows:

1972	\$ 201,665
1973	111,551
1974	80,498
1975	55,100
1976	Nil

## 8. CONVERTIBLE DEBENTURES AND SUBSCRIPTIONS RECEIVABLE

Effectively as of June 30, 1971 the Company sold \$200,000 of 7½% convertible unsecured debentures to certain directors and senior officers at a 4% discount from face value. The debentures mature on June 30, 1976. The debentures are convertible into common shares at the price of \$2.00 until June 30, 1973, \$3.00 until June 30, 1974, \$4.00 until June 30, 1975 and \$5.00 until June 30, 1976.

The balance of subscriptions receivable at June 30, 1971 is comprised of:

Net sale price of debentures	\$ 192,000	
Cash received	50,000	
Balance (received in August 1971)		\$ 142,000
Subscriptions due on senior employees' stock purchase (shares held by trustee)		12,180
		<u>\$ 154,180</u>

## 9. SHARE CAPITAL

During the year, 13,100 common shares were issued as follows:

3,800 Exercise of incentive stock options	\$ 3,800
9,300 Stock purchase	9,300
13,100	<u>\$ 13,100</u>

The Company has an incentive stock option plan which provides for the issuance of five-year options to officers and key employees at prices approximately market value at the date of grant. These options become exercisable on a cumulative basis 20% per year. At July 1, 1970 options to purchase 35,000 shares of common stock at \$1.00 were outstanding. During the year, options for 4,250 shares at a price of \$1.40 were granted; options were exercised for 3,800 shares and options were cancelled for 6,200 shares. At June 30, 1971, options for 29,250 shares were outstanding (25,000 until March 24, 1975 and 4,250 until April 23, 1976) at an average price of \$1.06 per share. There are 1,950 shares available for future grants.

The Company issued 9,300 shares of common stock to senior employees at the price of \$1.40 per share.

In addition, 100,000 authorized common shares have been reserved for possible issuance on conversion of the 7½% unsecured debentures (Note 8).

# COMTECH GROUP INTERNATIONAL LIMITED AND SUBSIDIARIES

## 10. CONTRIBUTED SURPLUS

Balance at June 30, 1970 .....	\$ 681,851
Premium paid on common shares issued during year .....	<u>3,720</u>
	685,571
Transfer to retained earnings .....	<u>568,714</u>
Balance at June 30, 1971 .....	<u>\$ 116,857</u>

The transfer of contributed surplus to retained earnings of \$568,714 represents the organization and finance cost of \$94,931 and the aggregate net loss (from operations, disposal of assets and shares) of \$473,783 on the ownership of Fibre Products from the date of merger in June 1969 to the date of disposal. In 1969, the Company made a transfer of \$280,414 from contributed surplus to eliminate the accumulated Fibre Products deficit at the date of its merger with Comtech Group Limited. After effecting these transfers, the retained earnings balance of \$30,500 relates entirely to the computer service segment of the Company.

## 11. DIVIDEND RESTRICTIONS

Dividends on the 5% cumulative preference shares have been paid to June 30, 1954. Arrears of dividends amount to \$38,165 at June 30, 1971 on the 4,490 shares outstanding. Since the Company failed to pay more than three consecutive half-yearly dividends on the 5% cumulative preference shares and more than four consecutive half-yearly dividends on the 3% non-cumulative preference shares, both classes of shares carry voting rights.

One of the subsidiary companies has unpaid cumulative preference dividends owing to minority shareholders in the amount of \$4,331.

## 12. INCOME TAXES

The Company accounts for income taxes on the tax allocation basis resulting in a credit to deferred income taxes of \$3,050. However, the Company has accumulated accounting losses of \$863,581 of which \$724,013 are available to carry forward for income tax purposes. These may be claimed in future years up to the following dates.

Amount of Tax Loss	Available to
\$ 601	1972
35,211	1973
262,540	1974
299,503	1975
126,158	1976
<u>\$ 724,013</u>	

## 13. COMMITMENTS

The companies are committed to annual realty and equipment rentals approximately \$128,000 until 1972 and \$33,000 thereafter expiring in various periods up to 1986.

## 14. STATUTORY INFORMATION

The aggregate direct remuneration paid or payable by the Company and its subsidiaries to the directors and senior officers of the Company was \$99,859 (\$115,095 in 1970).

Total interest paid on long-term debt amounted to \$56,283 (\$44,327 in 1970).

## 15. EARNINGS PER SHARE

	1971	1970
Income (loss) on continuing operations .....	<u>.06</u>	<u>(.02)</u>
Income (loss) including loss on discontinued operations before extraordinary items .....	(.03)	—
Net income (loss) after extraordinary items .....	<u>(.85)</u>	<u>.18</u>
Average number of shares outstanding .....	748,463	698,428

Earnings per share are calculated, after dividends on the 5% cumulative first preference shares, based upon the weighted monthly average number of shares outstanding during the year. Had the common shares reserved at June 30, 1970 and 1971 for all then outstanding options and conversions been actually issued from the first of the year, there would have been no dilutive effect on earnings per share.







